

# CHINA AT SIXTY

**Pranab Bardhan**

[China is in many ways a land of contradictions, confounding outside observers. And such contradictions are nowhere more obvious than in China's economy: a market-driven allocation of resources overseen by the Communist Party. But as Berkeley Economics Professor Pranab Bardhan notes, the contradictions lie at an even deeper level. Simply establishing private ownership of some of China's largest companies is decidedly serpentine and many of the owners have familial ties with, or are themselves members of the Party. Moreover, many state-owned enterprises are controlled by political families. Such fuzzy lines between political connections and business have led to particularly egregious abuses of power that are precisely the predatory tendencies of capitalism that the Chinese Communist Party originally sought to defeat. Indeed, as Bardhan points out, many government officials now find it difficult to control their own colleagues' venality, collusion, or depredations. But as some assert, as long as control of the economy remains with the state, such ills will continue to plague China. Though Chairman Mao believed that contradictions were the nature of society, it is doubtful he would have imagined all the contradictions that obtain in China's society today.]

As the sixtieth anniversary of the People's Republic of China approaches, one is prone to reflect generally on its dramatic recent history, including the historic irony of the development of today's arguably most vigorous capitalism in an avowedly communist country. The contradictions involved here are much more than were dreamt of in Mao's philosophy when he famously speculated on the nature of contradictions, first in a 1937 essay, where he stated: "The law of contradiction in things, that is, the law of the unity of opposites, is the fundamental law of nature and of society."

While the Party retains the monopoly of power, the market mechanism is the major allocator of resources in the Chinese economy – much like it was in Taiwan during the authoritarian days of KMT, an anti-communist party organized on quasi-Leninist lines. While most people agree that the private sector is now the more dynamic part of the Chinese economy and creates most of the jobs, to find out how much of the (non-farm) economy is actually under private ownership is not straightforward: it is not easy to classify Chinese firms by their ownership or to distinguish between private and public or semi-public control rights. Even in China's most famous private companies, Lenovo and Huawei Technologies, the ownership structure is quite convoluted, as Yasheng Huang indicates in his book *Capitalism with Chinese Characteristics*.

This is, of course, part of the legacy of the development of the Chinese private sector under the shadow of the Party-controlled state. As late as 1988, private firms with more than 8 employees were not permitted. Many private firms operated below the radar and used various subterfuges and covert deals with local officials, as they adapted themselves to the changing permissible mores. Some of them used to be called "red-hat capitalists", sometimes hiding under the façade of local collectives. Only since the late 90's did they slowly take off their red hats and start coming out of the closet. Many of the smaller and regional State-owned Enterprises (SOE's) were privatized and often their managers became the new owners. Today, probably more than half of the non-farm output (though not of fixed capital investment) is primarily privately owned or controlled. Currently about one-third of the private entrepreneurs are members

of the Party (including “xiahai” entrepreneurs who are former officials); membership helps them get state finance, and more protection and legitimacy.

Of course, it is well-known that some of the entrepreneurs are in fact friends or relatives of Party officials. ( An article in *Der Spiegel*, 27 February, 2007, reported a finding by the State Council of the Academy of Social Sciences and the Party’s Central University that of the 3320 Chinese citizens with a personal wealth of 100 million yuan or about \$14 million, 2932 were children of high-ranking Party officials). Many SOE’s are also controlled by powerful political families. Thus there is a new political-managerial class, which over the last two decades has converted their positions of authority into wealth and power. The vibrancy of entrepreneurial ambitions combined with the arbitrariness of power in an authoritarian state has sometimes given rise to particularly corrupt or predatory forms of capitalism, unencumbered by the restraints of civil society institutions. Perhaps nowhere has the predation been as starkly evident as in land seizures both in cities and the countryside. In the real estate boom of recent years, for example, the commercial developers in cahoots with local officials have bulldozed old city neighborhoods, residents waking up in the morning to find that their house has been marked for demolition with the Chinese character “chai” – meaning raze – painted in white, with hardly any redress or adequate compensation available.

This corrupt or predatory form of capitalism has also some obvious global implications. When foreign companies try to invest in China or Chinese companies try to acquire holdings abroad the decision-making process can be vitiated by arbitrary political interference, underhand dealings, kickbacks and influence-peddling. Even in matters of foreign aid in Africa a recent *New York Times* report points to the opacity in the activities of politically well-connected Chinese foreign-aid contractors.

While the state has relaxed its earlier control over prices and allows markets and profit-making to be the major organizing principle of domestic economic life, it is still predominant in the capital goods sectors and in transportation and finance. Some of the SOE’s are now important players in the global market competition. In general, in recruiting professional managers, broadening their investor base, and shedding their traditional social and political obligations, many SOE’s do not conform to the usual stereotypes about SOE’s. The state still controls the larger and often more profitable (high-margin, monopolistic) companies in the industrial and service sectors. The state’s role in regulating the private sector also goes far beyond the usual functions in other countries. Apart from exerting indirect control rights in private firms, during the current global recession some SOE’s, flush with abundant loans from state banks, have even taken over some of the financially-strapped small and medium-size private enterprises. As a senior Chinese banker commented (quoted in the *Financial Times*, August 24, 2009), “It’s quite hard to compete when you’re playing against the referee.”

An important question arises in cases where an enterprise is managed on essentially commercial principles, but the state still has control rights over a large share of the assets: is this a capitalist enterprise? Some may describe it as capitalist if the principle of shareholder value maximization is followed (though

this principle is not always followed in capitalist countries – say, in Japan or Germany). Others may point out that as long as substantial control rights remain with the state, which is subject to ever-malleable and potentially arbitrary political considerations, the internal dynamic logic of capitalism is missing, and politics take command. In late 2008, when China's richest man, Huang Guangyu was arrested, many thought that his biggest crime was that he was getting too powerful for the leaders' comfort (shades of Putin's Russia).

Nevertheless, it is probably reasonable to guess (though it may not be enough to reassure the global business community) that while the Party can undo individual capitalists at short notice, it will be much more difficult for the leadership to unravel a whole network of capitalist relations, by now thickly overlaid with various vested interests knotted with "guanxi" ties. Individual entrepreneurs have a clientelistic relationship with the state, but the state, for all its relative autonomy, is now sufficiently enmeshed in a profit-oriented system that has been identified with legitimacy-enhancing international economic prowess and nationalist glory, a tiger that the political leadership may find difficult to dismount. At the local level, the central leadership, even while holding the important instrument of career promotion for local officials, often finds it difficult to rein them in as they collude with local business to commit some of the worst capitalist excesses (in land acquisitions, product safety violations or toxic pollution). In any case, by an official account, the Communist Party composition itself has drastically changed, the majority of members now are no longer workers or peasants, but professionals, college students and businessmen. Such are the ambiguities and contradictions of Chinese capitalism that Chairman Mao never foresaw, nor did the capitalist corporations in the West now dealing with this strange hybrid. [25.9.2009] □□□